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Q1 2007 **Countrywide Financial** Corporation Earnings **Conference Call** - Final

OPERATOR: Ladies and gentlemen, thank you very much for standing by. We do appreciate your patience today while the conference assembled and good morning. Welcome to the **Countrywide Financial** Corporation's first-quarter 2007 earnings **conference call**.

If I may have your full attention, please note that during this teleconference, Countrywide's management may make forward-looking statements within the meaning of the federal securities laws regarding their beliefs, estimates, projections and assumptions with respect to, among other things, the Company's future operations, business plans and strategies, as well as industry and market conditions, all of which are subject to change.

Actual results and operations for any future period may vary materially from any past results discussed during today's teleconference. Factors which could cause actual results to differ materially from historical results or those anticipated include, but are not limited to, those items described in the first-quarter press release and detailed in documents filed by the Company with the Securities and Exchange Commission from time to time. The Company undertakes no obligation to publicly update or revise any forward-looking statements.

In just a moment, we will get right to the management team's prepared remarks, but first I will cover just a few housekeeping items. Now, namely, at this point, we do have all of your phone lines muted or in a listen-only mode. However, later, there will be opportunities for your questions and if you would like to queue up, we certainly invite you and encourage you to press star one on your phone keypad. (OPERATOR INSTRUCTIONS).

As a reminder, today's call is being recorded for replay purposes. We ask that you stay online at the conclusion of our conference to receive that replay information. So with that being said, we will get right to this first-quarter agenda. Here is our host, Countrywide's Chairman and Chief Executive Officer, Mr. Angelo Mozilo. Good morning, sir and please go ahead.

ANGELO MOZILO, CHAIRMAN & CEO, **COUNTRYWIDE FINANCIAL** CORPORATION: Thank you very much, Brent and good morning. Good morning and welcome to Countrywide's earnings teleconference call for the first quarter of 2007. Joining me on the call today are David Sambol, our President and Chief Operating Officer; Eric Sieracki, our Chief Financial Officer; Kevin Bartlett, our Chief Investment Officer; Carlos Garcia, our Chief of Banking and Insurance; Tim Wennes, the President of Countrywide Bank; Ron Kripalani, our President of Countrywide Capital Markets; Bob James, our President of Balboa Life & Casualty; John McMurray,

our Chief Risk Officer and Anne McCallion, our Chief of Financial Operations and Planning.

If you have not done so already, please download the first-quarter supplemental presentation from our website. Dave Sambol and John McMurray have prepared this very detailed slide deck to walk you through the various subprime and credit cost impacts to our earnings this quarter, as well as an update on the subprime and Alt-A markets.

Since most of you already saw this morning's press release, I will not spend the time going through all of the information contained within it. Instead, for those who may be traveling or haven't had a chance to read it, I will briefly summarize the earnings results so that we can be sure to allow plenty of time for Q&A at the end.

So to quickly recap, diluted earnings per share were $0.72 for the first quarter of 2007, which compares to $1.01 for the fourth quarter of 2006 and $1.10 for the first quarter of last year. While the Company's core operations delivered what was otherwise a strong quarter, earnings were impacted by charges relating to our subprime activities, as well as increases to our loss reserves and related asset valuation adjustments stemming from higher delinquencies and softer housing markets.

These impacts equated to $0.41 in earnings per diluted share related to subprime operations and $0.14 in earnings per diluted share related to other credit costs relative to the fourth quarter of 2006. Excluding these impacts, our Production sector delivered strong volume and margins for both prime first and home equity loans, which accounted for 93% of our total mortgage banking originations. And servicing sector margins, excluding impairment of retained interest, were also strong.

On a consolidated basis, Countrywide's residential lending operations continue to grow marketshare with the first-quarter production representing over 18% share, which is the largest we've ever had and our Servicing portfolio representing 13% of residential loans outstanding.

In addition, our pipeline heading into the second quarter is very strong at $69 billion, up 21% from the fourth quarter of 2006 and up 8% from the first quarter of last year.

The loan production sector pretax earnings were $139 million, which compares to $421 million for the fourth quarter of 2006 and $284 million for the first quarter of last year. In the loan servicing sector, we had a pretax loss of $69 million for the first quarter of 2007, which compares to a pretax earnings of $9 million for the fourth quarter of 2006 and $249 million for the first quarter of 2006.

Our increasingly diverse business model has been generating more than half of our earnings from businesses other than mortgage banking, as was the case in 2006 and in the first quarter of 2007. Net interest margins increased in our Banking Operations and our Capital Markets and Insurance segments both generated sequential quarter pretax earnings growth.

Banking Operations pretax earnings were $294 million for the first quarter of 2007, which compares to $346 million for the fourth quarter of 2006 and $331 million for the first quarter of 2006. Capital Markets delivered pretax earnings of $132 million in the first quarter of 2007, which compares to $99 million for the sequential quarter and $156 million for the first quarter of last year. The Insurance segment pretax earnings were $180 million in the first quarter of 2007, which compares to $75 million for the fourth quarter and $65 million for the first quarter of last year.

Looking forward, we believe that considerable risks remain in the mortgage marketplace as described in our press release. While the balance of 2007 is expected to be challenging, we continue to believe that current market conditions will result in opportunities in the form of further industry consolidation.

We also believe that the Company is well-positioned to capitalize on these opportunities, which have strengthened Countrywide's franchise and result in accelerated future marketshare and future earnings growth.

We updated our guidance for 2007 and expect diluted EPS to range from $3.50 to $4.30. This compares to our previous guidance provided on January 30, 2007 of $3.80 to $4.80. The revision reflects our actual performance in the first quarter and our expectations for the next three quarters.

And finally before Dave and John take you through the financial implications of current industry conditions, let me take a moment to talk about how we are responding to the increased delinquencies among some of our subprime borrowers.

Countrywide's mission always has been and always will be centered on sustainable home ownership. As such, we are focused on taking whatever steps are possible and that are sensible from a financial perspective to assist borrowers who are having difficulty making their payments. It is not something new for Countrywide. It is what we have always done and we have been very successful doing throughout our nearly 40 years history.

Our 50,000 plus employees work diligently every day to make the American dream of homeownership available to as many people as possible and I want to thank them for that effort once again. We also support the efforts of policymakers such as Senator Dodd to bring lenders, regulators and advocates together to identify market-based solutions to some of the issues that have been in the news lately. We look forward to continuing our participation in these discussions. And we do not believe a legislative solution is neither necessary nor appropriate. And now let me turn this over to David Sambol. David?

DAVID SAMBOL, PRESIDENT & COO, **COUNTRYWIDE FINANCIAL** CORPORATION: Okay. Thanks, Angelo. Because of the notable impact to the quarter from subprime and increased credit costs, we have put together a supplemental presentation -- as Angelo mentioned, it is on our website -- to drill down into these two areas in more detail. I will walk you through an overview of the subprime environment and what has transpired from our perspective, the adjustments that Countrywide has made in that part of our business and what we view the business to look like looking ahead. And then I will hand it off to John McMurray, our Chief Risk Officer, who will talk about the topic of credit risks and how we manage price and reserve for credit risk.

So on slide 4 of the presentation on the website, in terms of overview as to what has transpired in the subprime markets, the current turmoil in subprime was precipitated in our view by a convergence of several things; expansion of program and credit guidelines in the industry over the last several years, followed by a flattening of home price appreciation and in fact, declines in home prices in some markets over the last year, which in turn has resulted in increasing delinquencies and defaults in the sector, particularly in the last several quarters.

These conditions were further exacerbated by significant overcapacity and competition in the subprime sector and really the resulting lack of profitability even before increased credit costs and losses. So all of these factors converged to create the disruption and the turmoil in the subprime market that we have seen in the first quarter.

To date, more than 30 monoline subprime lenders have exited the business since the end of the year, impacted by lack of profitability, increased credit-related losses and ultimately lack of liquidity to finance their ongoing business.

In the secondary markets for subprime loans and securities, we have seen a significant widening of spreads, of investor yield requirements in the first quarter. However, I would point out that over the last week or two, we have seen buyers coming back into the market and we have seen spreads tightening somewhat coming back in as well.

In reaction to all this, there has been a significant industry tightening of credit and underwriting guidelines over the last several months and really a reversal of much of the expansion that occurred over the last several years.

In terms of impact of all this looking ahead is that we certainly expect to see subprime volumes fall from their levels in 2006. It will be a much smaller market. Estimates range from a drop in volumes of between 30% and 50% relative to '06 volumes and the exact drop will be in part a function of the outcome of regulatory and possibly political uncertainty that could impact volume.

And notably, the remaining players in the sector today tend to be the larger financial institutions, large banks like Countrywide and JPMorgan Chase and Washington Mutual and Wells and also the Wall Street firms. Players who we view to be more rational and responsible.

So looking ahead, while we expect the subprime market to be smaller, we also expect for it to be less crowded and more rational and hopefully more profitable.

On slide 5, in terms of the adjustments that Countrywide has made in response to market conditions, I mentioned that industry guidelines have been heightened, but we have also significantly tightened our own credit guidelines and programs. For example, materially restricting 100% loan-to-value financing, carving back materially reduced documentation programs, particularly on the higher LTVs, eliminating subprime second mortgages, which have particularly been impacted by liquidity and loss in value in the market.

We have also enhanced our operating controls and procedures and our workflows and protocols to improve credit quality, especially as it relates to the way we handle investor properties, both investors who are applying to acquire a property, as well as transactions involving the sale by an investor of an investment property. And so we have made significant changes with respect to both controls and to guidelines.

Also importantly, the carrying value of our existing investments in subprime asset and subprime residuals have been written down as we laid out in our press release to provide for more conservative higher loss projections and also higher yields on the asset going forward.

And then pricing of new loans that we are originating have also been adjusted to provide for more conservative loss assumptions, higher yield on our retained interest from future originations and greater origination margins as well.

On slide number 6, we have put this here as a visual as to what our future production will look like relative to our historical production and we have chosen the fourth-quarter volume as the point of comparison and we have looked at our recent application activity for the purpose of projecting what second-quarter volume might look like and that is what is highlighted on this slide.

As you can see, we expect volumes going forward or at least second-quarter volumes to be down by 25% to 50% from our subprime funding volumes in the fourth quarter. We expect that the percentage of subprime volume to Countrywide's overall volume will drop to the 4%, 5%, maybe 6% range, down from 8% of total volume, which is what it was running in the fourth quarter last year.

With respect to the profile of the production that we are now originating, in the fourth quarter and in 2006, it was the case that approximately 25% of all of the subprime loans we were doing were 100% LTV loans. That percentage will drop to just a negligible amount, less than 5%. Of the 100% loans that we were doing then, approximately 90% were adjustable rate mortgages. We have eliminated ARMs and 100% financing going forward. We will only be doing fixed-rate loans on high LTV financing or 100% financing.

In terms of reduced documentation, I mentioned that we have curtailed our guidelines and offerings of reduced documentation loans. Reduced documentation loans are presented approximately 35% of the loans, which were above 90% LTV. We have eliminated, reduced docs above 90%. Average LTVs will drop. Our average LTV was approximately 85% last year. It will be below 80% looking ahead and notably, first-time homebuyers, a significant portion as I am sure you are aware of our subprime production was purchased on money mortgages and a significant portion of that was to first-time homebuyers. In fact, first-time homebuyer loans represented approximately 22% of our overall subprime volume in the fourth quarter. That will drop to approximately 5%.

In fact, if we just look at first-time homebuyers as a percentage of the purchase money mortgage business that we were doing in the subprime sector, that was 60% of our purchase business in the fourth quarter and that will fall by approximately 75% down to 60% of purchase subprime volume. So that is some color as to the impact of the changes that we have made.

On the next slide, we have highlighted the impact both of write-downs to our subprime investments and to our production profitability in the first quarter stemming from the turmoil in the subprime markets. And as you can see, we have quantified that the quarter-over-quarter impact was approximately $400 million stemming from both write-downs in our residual investment and reduction in origination margins and gain on sales.

With respect to the impairment in our subprime residual assets, that approximated $212 million during the quarter. We had a write-down on loans that were unsold, subprime loans, predominantly second mortgage loans at quarter-end of approximately $218 million.

We have estimated that with respect to that which was sold during the quarter relative to sales during the fourth quarter that the lesser execution quantified to approximately $120 million and then those hits were offset by hedge gains that we enjoyed on -- hedges that we had on against credit spread widening, notably ABX hedge gains. So that is the impact to the quarter relative to the subprime conditions.

On slide 8, there has been a lot of talk about contagion or spillover from subprime to Alt-A and so we thought we would comment a little bit on that market and Countrywide's views and exposure to Alt-A. First of all, by way of description, Alt-A generally consists of loans to prime credit borrowers unlike subprime. FICOs generally in excess of 700 who don't qualify for traditional prime programs due to a variety of things; reduced documentation most notably and/or other layering of risk factors, maybe higher LTVs and higher loan amounts.

Now with respect to Countrywide's production, it is important to point out that approximately two-thirds of our Alt-A production is eligible for sale to the GSEs. And approximately 8% of Countrywide's volume that is not -- of the volume that is not eligible for sale to the GSEs, approximately -- it accounts for approximately 8% of our total volume.

Now, we have seen in the first quarter as has been the case in subprime, although to a far lesser extent, liquidity for subordinated securities impacted on our non-GSE eligible Alt-A loans and securities and spreads have widened there as well. Although, as I said, not to the extent that we have observed in subprime and like I commented in terms of what's happening today in subprime in the last week or so, we have seen significantly more demand for Alt-A securities and spreads have come in there as well.

In fact, in the first quarter, Countrywide had occasion to sell approximately $5 billion of our Alt-A production and on those sales, we would point out that we did not have to retain virtually any subordinated securities or interest. In fact, we capped a few million dollars worth of bonds representing less than 1% of that which we sold.

Also like the adjustments that we've made on subprime and that the market has made on subprime. We have seen credit tightening occurring in the industry and we have tightened our guidelines somewhat as well on the Alt-A side and I would point out that our rate sheets and our pricing fully reflect all the widening that we have seen in the markets.

So by way of summary on slide 9 relative to subprime, market conditions certainly have had an adverse impact

on our Q1 results. However, lesser competition and rationalization of credit guidelines and pricing are very positive implications of this market correction for the industry and for Countrywide.

As for Countrywide, we made all the necessary adjustments we believe to enhance profitability and to lessen our future exposure to the sector. Industry volumes will fall this year, but we expect the remaining volumes to be far more profitable than they were, particularly in the wholesale channel, which for us was really not generating very much profitability at all over the last year to two years.

We were operating at margins that were close to breakeven and we expect that in the coming quarters we will now see positive operating margins not only in wholesale, but in each of the channels in which we are still participating in subprime. And of course Countrywide has the liquidity and the capital and the infrastructure to take advantage of the structural changes that are taking place in this market.

As it relates to Alt-A, the conclusion there is that, at least for Countrywide, there has not been any material impact or spillover into Alt-A or for that matter into our prime business. In fact, if anything, spreads and demand for prime product have increased. Spreads have tightened and demand has increased.

And that is a quick overview of subprime and its impact to us this past quarter and with that, I will hand it off to John McMurray to talk about the topic of credit costs and credit risk.

JOHN MCMURRAY, CRO, **COUNTRYWIDE FINANCIAL** CORPORATION: Thanks, Dave. Let's turn to page 11. On pages 11 and 12, I provide an overview of our key credit risks. Page 11 is a geography showing how our primary credit risks manifest themselves on our income statement and balance sheet. Rows represent major risks, columns represent the financial statement treatment for each risk.

Let's take a look at each row. HFS is held for sale inventory. It is held on our balance sheet at LOCOM. That is the lower cost to market. The key point here is that these loans are marked rather than reserved. We do also use permanent impairments on some loans to reflect credit defect and/or delinquencies that are likely to be realized when the loan is sold. But, again, the key point here is mark rather than a reserve.

The second row down is HFI, which is held for investment portfolio. Here, we provide for credit losses in three ways; ALLL, which is an allowance for loan and lease losses. You can think of that as a traditional reserve. Secondly, through basis adjustments and then thirdly through the use of credit enhancements. By basis adjustment, I am talking about a charge that is then reflected to the loan's carrying value on the balance sheet.

Third major row down is residuals and, as most of you know, these are first loss non-investment-grade securities. The underlying loan collateral is largely subprime first liens and prime HELOCs. Losses for residuals are explicitly provided for as part of the residual valuation process.

The next major row is representation and warranty exposure. This arises from our securitization and loan sales

activities where we may be required to repurchase or indemnify as the result of a contractual breach. Future credit losses from this rep and warrant exposure is provided for via a reserve.

The fifth or second to the last row on page 11 is our Mortgage Reinsurance exposure. Countrywide provides mezzanine reinsurance to all of the major mortgage insurers on loans that we originate or purchase. Credit losses here are provided for using a reserve that appears as an accrued liability on our balance sheet, so you are not going to see it in the traditional reserve category.

And then finally on page 11, our Servicing Advances, which are primarily associated with either FHA or VA loans. VA no-bid is an example of a credit loss that we would incur on this row. These credit costs are also provided for via a reserve and this is going to appear also in accrued liabilities on the balance sheet.

All right, let's turn to page 12. On page 12, the rows match what you saw back on page 11. Let me describe what is in the columns. For each of the major columns, we show values for both the first quarter of 2007, as well as the fourth quarter for 2006, so you can get some sense of how the two quarters compare to one another.

All right. Let's go column by column. Balance sheet assets are the first two columns on the left and this is just simply the carrying value of these assets on our balance sheet. So as an example, HFS is just the lower cost market value of our inventory. HFI is our investment portfolio that is held at cost less the reserves that we have booked against that minus the basis adjustments that I talked about a moment ago.

On rep and warranty, obviously there is no balance sheet value there because those assets have been sold, but we do retain risk on that. The next group of columns is the underlying UPB. This is the unpaid principal balance underlying the loans for each asset or risk category. Continuing to move left to right, provisions/earnings charge is the amount that we recognized on our income statement. You will note that some of these charges are to a loss provision and other charges are charged directly to gain on sale, so you will see a description of how this works back on page 11.

And then finally over at the far right, the last two groups -- the last group of two columns represents the amount we have on our balance sheet for future losses. I will elaborate on this in a few more pages as we go through the major risk guidance.

Now that we have this basic overview, let's take a look at the individual risk categories. Pages 13 and 14 cover the HFI or held for investment category. Starting on page 13, most of our HFI exposure resides on the bank balance sheet where we originate and purchase prime mortgage loans for investment.

In addition to the bullet point that emphasizes our investment approach where we emphasize higher credit quality loans, you should also know that we consider market risk and expected returns when selecting assets for this portfolio. HFI assets outside the bank are quite different than those inside the bank. These assets have traditionally come about as the result of our government loan rewarehousing program, repurchases or transfers from HFS to HFI. The recent transfer of subprime seconds to HFI is an example of loans moving from our held for sale in-

ventory portfolio over to our investment portfolio.

In the bank, credit losses in our HFI portfolio are provided for using a traditional ALLL reserve and credit enhancements. The ALLL reserve covers our lifetime estimate for losses on loans that are now 90 plus past due, as well as our estimate of losses for loans we expect to become 90 days past due some time over the next 12 months. Credit enhancements in the bank are typically comprised of mortgage pool insurance policies.

Outside of the bank, basis adjustments are used when a loan first enters a loan either as a repurchase or a transfer from HFS. This basis adjustment reduces the loan's carrying value to reflect defects and/or the loan's delinquent status. Credit enhancements outside the bank are typically government and by government, I mean FHA or VA insurance or guarantees.

Finally on this slide note that we increased our default estimates in the first quarter, which was one of the drivers behind the larger provisions that we took during the quarter.

All right. Let's turn to page 14. Page 14 provides more information on our HFI portfolio, particularly for residential loans. We have the bank HFI portfolio on the top half of the page and the non-bank HFI portfolio on the bottom half of the page. The columns show UPB, that is the unpaid principal balance, then next, the percentage of each portfolio covered by a credit enhancement, the total and 90 plus day delinquencies and then the reserve for future losses.

For the bank, we also show an estimate of current loan to value ratio, that is what LTV stands for, and then the original FICO for these loans. In addition to the ALLL, the bank reserves here shown also include reserves we have booked for undrawn HELOC advances that appear as other liabilities. So these are reserves that we have taken against HELOCs for amounts that have not yet been drawn, but that we expect to be drawn in the future and that we also expect to see a delinquency on.

For the non-bank section at the bottom of the page, reserves include basis adjustments and ALLL. Let me point out a couple of relevant facts for delinquencies. First, these delinquencies are based on loan balances that are past due or in foreclosure, so it is both delinquencies plus in foreclosure. Second, they are calculated using the MBA standard. Some institutions report delinquencies using the OTS standard, which usually results in a lower reported delinquency, particularly for first liens.

Let me amplify the differences between MBA and OTS standards using the Countrywide servicing portfolio as an example. The total delinquency for the servicing portfolio at the end of March was 4.9% using the MBA standard. If we recalculate for this same portfolio at this same point in time using the OTS standard, the delinquency is 2.6%. So again, same set of delinquencies, it's 4.9% under one standard, 2.6% under another standard.

Two more quick examples. For 90 plus for the total servicing portfolio, 1.7% using the MBA approach versus 1.4% using the OTS approach. And then finally, I wanted to use non-prime first liens as my final example. Here, at the end of March, the total delinquencies were 19.8% using the MBA approach versus 11.6% using the OTS

approach. So there can be significant differences there.

Finally, on this page, we show the reserve to 90 plus delinquency ratio that some of you track. Keep in mind particularly for the non-bank portfolio that that is going to include basis adjustments as well as the traditional ALLL reserves. And then we also show the percentage of 90 plus loans that are covered by credit enhancements.

All right. Let's move on to residuals. Residuals begin on page 15. As I mentioned earlier, these mainly come about as the result of subprime and HELOC securitizations. They are first loss securities. Estimates of future losses are incorporated into each residual's valuation. If our estimate of future losses is higher than our estimate of our residual revenues then the residual will have no carrying value on our balance sheet and we in fact have residuals where we have no carrying value even though there are active loans underlying those securities.

As the second bullet point mentions, we mitigate losses on residuals through the sale of these assets, through the sales of NIMs and a NIM is a portion of residual's future cash flows and through mortgage insurance. Like HFI, higher default expectations were used during the first quarter, which also resulted in write-downs on many of our residuals, particularly in subprime and HELOCs.

The second to the last bullet point on this page is an important one and the point is that residual exposure is limited to the balance sheet carrying value.

Finally, on page 15, I make note of the underwriting guideline changes Dave described to you a few minutes ago. We do expect these changes to reduce losses on future originations.

On page 16, we have more information on our residual exposure. The residuals are split into two broad categories. The first major row are first liens, which are primarily subprime and then second liens, which are primarily prime HELOCs. The first two columns of numbers show balance sheet carrying values for the first quarter of 2007 and for the fourth quarter of 2006. Notice the carrying of values and thus exposures are down quarter-over-quarter despite adding new residuals for the first quarter.

We also show UPBs and pool factors in the center columns, then delinquencies, which again are calculated using the MBA standard and then finally, embedded losses in both dollars and percent for the two columns at the far right. Note that the embedded losses are after the effect of mortgage insurance. So in both our HELOC securitizations and in our subprime securitizations, we will often incorporate mortgage insurance into those structures and that will absorb some of the losses that we expect to take.

Also note in the bullets that prior to the effect of mortgage insurance, the loss percent for subprime vintages -- for all of our subprime vintages I should say would be around 7% rather than the 6% that you see in the upper right that reflects the after MI losses.

Let me make a couple of comments with respect to recent vintages. First, note that our subprime residual expos-

ure for the 2006 vintage is limited at $47 million. Second, while we do expect 2006 to be one of the worst vintages we have ever seen, we don't yet know how much of the initial poor performance we have observed will ultimately split out between a steeper loss seasoning ramp versus simply a higher loss rate across the higher seasoning spectrum.

Recent observation have delinquency transition rates show some convergence for the 2006 vintages -- or 2006 vintage with earlier vintages suggesting that a significant portion of what we are observing is attributable to a faster ramp rather than simply higher losses across the entire expected life of those assets.

All right. Let's move to page 17. Page 17 outlines our rep and warrant exposure. We have a long history with this particular type of exposure that spans many different market and product types. The bulk of this exposure is created when we securitize and sell loans and is generally related to loan manufacturing issues. Most rep and warrant breaches have historically appeared in the first 12 months of a loan's life.

Let me also give you the basic algebra for this exposure. And the basic algebra is that first the default rate we tend not to see repurchase requests on loans that haven't defaulted, so it is the default rate, times the severity, times the breach rate -- we are not go to repurchase a loan that there is no breach on -- times the repurchase request rate -- someone has to request the repurchase -- and then finally times one minus the request recission rate. So there is a fair number of requests that come in that ultimately do not get repurchased after we have taken a harder look at it.

In addition to traditional rep and warrant exposure, we also have EPD or early payment default exposure. EPD is primarily associated with whole loan sales and tends to be short term in nature; even shorter term than the rep and warrant breaches I mentioned a minute ago. We have never been as reliant on whole loan sales as some lenders and thus have had less EPD exposure. Although where we do have it, we established a reserve. Also, as we note on this slide, this exposure for our subprime business is now de minimis.

All right. On to page 18 where we outlined the exposure of our Mortgage Reinsurance business. This program started in 1995 and we have had no losses to date on this exposure; though the event space has been favorable. By event space, I mean that house prices, the general economy, prepayments, etc., have been favorable while these books were outstanding. We don't expect this environment to continue into the future and therefore continue to maintain a reserve against this exposure.

Here, we use a long-duration approach for calculating reserves, which allows us to incorporate a life of loan estimate into our reserve. The resulting loss percentage is booked as a provision when we recognize premium income. One important mind -- one important point to keep in mind here is that premium income is recognized as it is received. This is not an asset where future cash flows are present value.

Let me finish this page by commenting on the release of our 2003 book year reserves, which began in the fourth quarter and then continued into this quarter. This release was done in accordance with our established reserve policy and was the result of several factors, the most notable being prepayments. Because prepayments were

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faster than what we expected on this book of business, there is now a very low pool factor outstanding and based even on stress scenarios, we do not expect to pierce our entry point. In other words, our mezzanine layer, so the reserves were relieved. We also corroborated our internal work with external market bids prior to relieving the reserves.

This concludes my portion of the presentation, so let me turn the call back over to Angelo and Dave.

ANGELO MOZILO: Thank you very much, John. We are now ready, Brent, for questions and if you can open up the mics for questions, I would appreciate it.

OPERATOR: Indeed, I would be happy to and thank you very much, Mr. Mozilo and our team today for that update an overview. (OPERATOR INSTRUCTIONS). Bob Napoli, Piper Jaffray.

BOB NAPOLI, ANALYST, PIPER JAFFRAY: Thank you. Good morning. A question on the bank credit quality and kind of the outlook and that presentation was very helpful. Thank you very much for the additional disclosure. The provision level that you saw this quarter -- the ramp-up and obviously tied to credit. First of all, were you surprised by the amount of the credit weakening? Secondly, you did some reserve building. The provisions doubled in the current quarter. Do you expect the provisions to continue to need to ramp up and how much more weakness do you expect in nonperforming loans?

ANGELO MOZILO: Bob, let me turn this over to Carlos Garcia who will answer that question. Carlos?

CARLOS GARCIA, CHIEF OF BANKING & INSURANCE, **COUNTRYWIDE FINANCIAL** CORPORATION: Let me start talking about what is happening with NPLs in the bank. The Banking Operation's NPLs or nonperforming loans increased by $175 million during the quarter and this action represented a decline in the NPL number from a long growth rate from the prior quarter. It was a decrease of around $7 million in that growth rate. The increase in these nonperforming loans over the past two quarters has been driven really by ongoing seasoning of the portfolio, as well as by the condition of the housing market, which, as you know, has had a greater impact on California delinquency rates.

Having said that, the growth in the bank's delinquency rates slowed significantly in California, as well as outside California in Q1 and despite the growth in California delinquencies, bank loans and foreclosure remained well below prime industry foreclosure rates overall.

The seasoning of the bank's portfolio is being influenced by the reduction in the size of the portfolio in this current environment and by the fact that the portfolio is in a phase or an age of delinquency formation that is usually the steepest. As you pointed out, our provision for the first quarter did double and it is covered probably four times the level of charge-offs. By the way, charge-offs in the first quarter were driven primarily by our HELOC portfolio, which represents about 18% of the portfolio.

The increase in the provision was really largely due to increasing our reserve for future default in recognition of the recent delinquency formation trends, coupled with our expectation that the softness in the housing market is going to continue for some time. The net result was that the loss reserves for loans held for investment in the bank grew by approximately $100 million to $331 million, including a reserve that we have for undrawn HEL-OC lines. This reserve covers approximately two times the charge-off rate, the annualized charge-off rate that we are seeing in the first quarter.

In addition, as you know, the bank maintains credit enhancements on its pay options and second lien proposals and that credit enhancement now protects approximately $23 billion of loans, including 26% of the loans that are in the nonperforming category. This insurance also by the way represents over $1.5 billion in coverage for potential future claims.

Despite the higher provision and the growing mortgage insurance coverage, the bank still reported a return on equity in excess of 14% in Q1 and absent a worsening in the housing or employment markets or in recent non-performing loan formation trends, events that would lead us to further revise our future projections of defaults, future provisions should primarily be a function of the growth in nonperforming loans during those reporting periods. So I would expect, absent again a worsening of the environment, that the provisions should come down in the future. And as I noted earlier, the quarterly dollar growth in nonperforming loans applies in Q1.

ANGELO MOZILO: Thank you, Carlos. Bob, does that answer your question?

BOB NAPOLI: Yes. And there was just one other question and I will open it up for everybody else. Did you hold -- I don't see -- are you holding for investment purposes any subprime? Did you transfer any subprime or subprime seconds and if so, how much -- how much subprime are you holding, did you grow the held for sale on subprime, how much is still sitting out there?

ANGELO MOZILO: If you're talking about the bank, the bank holds no subprime.

BOB NAPOLI: No, no, I know, but on -- outside of the bank.

DAVID SAMBOL: Yes, Bob, this is Dave Sambol. We did, at the end of the first quarter, transfer subprime second mortgages from the held for sale category to the non-bank HFI category, which explains the growth on the one schedule that John McMurray walked you through. Motivation behind that is that the levels that we saw in the market for subprime were so distressed and far below economic value that it really made more sense for us to pull that out of HFS and to put it into the HFI category. Let me get the principal balance applicable to those seconds.

JOHN MCMURRAY: The principal balance is $900 million.

BOB NAPOLI: Okay.

DAVID SAMBOL: And Bob, the right down that we made reference to and the earnings impact from subprime applicable to unsold inventory at the end of the quarter predominately related, the $200 some odd million, predominately related to impairment on the subprime seconds that we took at that we wrote down before transferring them to the HFI category.

BOB NAPOLI: Great. Thank you.

JOHN MCMURRAY: That amount of impairment by the way was $187 million.

BOB NAPOLI: Okay.

OPERATOR: Fred Cannon, KBW.

FRED CANNON, ANALYST, KBW: Thank you. This is really a follow-up on the bank question that Bob was asking. I noticed that the MBS securities on the balance sheet went up by about $6 billion and that appears to have been growth primarily in the bank if I'm not mistaken, from the bank schedules that you guys provide. I was wondering if you could give us some color on that security investment increase, kind of what those -- what kind of securities those might be and I also noted that the yield on the securities portfolio at the bank jumped about 64 basis points in the quarter and if that is related to that securities investment.

CARLOS GARCIA: The securities portfolio of the bank is just of AAA mortgage-backed securities primarily related to either 30-year collateral where we take the first bond, the first cash flow bond that has a very short duration, or to pass through hybrid securities. And these securities are obviously a very high credit quality, and what they really represent is a source of reliable assets for us, particularly in this current environment where credit considerations are key.

They also provide predictable returns. They carry very low risk-based capital requirements and (inaudible) they're a strong source of liquidity. And we are viewing the purchase and growth of this securities portfolio really to be a transitional investment strategy during the current environment.

FRED CANNON: I guess as a follow-up then, that yield on that portfolio moving up 64 basis points, I was wondering if you could comment on the kind of yield that you were getting on the investments to get that kind of linked-quarter growth?

CARLOS GARCIA: Acquiring those securities, you know, 70 to 80 basis points spread to our cost of funds, and that translates based on 6% capital to about a 10% ROE. But based on risk-based capital, it is much higher returns. So we view them as a very good investment, given all the considerations.

UNIDENTIFIED COMPANY REPRESENTATIVE: Is that number correct, the 64 basis points?

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FRED CANNON: I was just looking at the yield on the other assets, and the most recent quarter was 5.45% versus 4.81% in the fourth quarter from the schedules that you guys provide.

ANGELO MOZILO: I'm looking at the brain trust here to see if anybody can reconcile it -- anybody can figure out that number?

FRED CANNON: I can come back to you guys on that.

ANGELO MOZILO: We will look at it and see if we can come up with it before the call ends.

FRED CANNON: Just one more quick question, Carlos. I noticed that the capital, the equity level, came down at the bank from about $6.3 billion to $5 billion at the end of the quarter. Is that due to the switch to the thrift charter, and I was wondering, did you basically dividend up that equity to the holding company?

DAVID SAMBOL: Let me answer that. No, Fred, I think starting in this quarter -- and we are going to evolve this in subsequent quarters -- we are going to start reporting capital and allocating capital to our segments based on a predetermined cap allocation paradigm, where in the case of the bank we are going to just allocate capital based on the regulatory requirement, and show excess capital being retained in the parent. And you are going to see us reporting returns on that basis, and our reporting formats will begin to modify accordingly.

FRED CANNON: Okay. So I shouldn't read into anything that is dropping the equity that you report on the bank schedule?

DAVID SAMBOL: No, it's just a segment allocation of capital based on what is required rather than what we might be retaining in the legal entity.

FRED CANNON: Okay. So that is not a regulatory capital number? Equity?

DAVID SAMBOL: No.

FRED CANNON: Okay. Thank you very much.

OPERATOR: Ken Posner, Morgan Stanley.

KEN POSNER, ANALYST, MORGAN STANLEY: Hi, thank you. I wanted to ask just a quick question on one of the slides that you showed, which I will also say were very helpful. Thank you. You showed I think a 6.3% loss assumption discounted in the subprime residuals. And I was wondering if you could just give some color about how that assumption varied for the '05 and prior books versus the '06 books, and what would be reasonable to be assuming, you know, for the '07 book and going forward?

DAVID SAMBOL: Sure. Well, obviously, on '06 it is higher than the average --.

ERIC SIERACKI, CFO, **COUNTRYWIDE FINANCIAL** CORPORATION: You can talk about what the expected losses were for '06 if you want.

DAVID SAMBOL: All right. So, again, for '06, especially after we take out the effect of MI, you are going to be in the 7% plus range for losses going forward. That would be our estimate. Keep in mind there are lot of other moving parts in valuing those residuals. It is not just the level of expected losses but how those losses come in from a timing standpoint, prepayments obviously, the discount rate that we are using to PV that all back.

KEN POSNER: That's helpful, just to understand your views on the credit development. Thank you.

DAVID SAMBOL: Certainly.

OPERATOR: Ken Bruce, Merrill Lynch.

KEN BRUCE, ANALYST, MERRILL LYNCH: Good morning. You know, the first quarter obviously was very nasty because of the subprime spread widening, but if you peel away some of those numbers it looks that the prime business in particular was very strong. I was hoping you might be able to provide some additional clarity into what is driving the prime margins up quarter over quarter, and as you pointed out were robust and you're seeing more demand. But if you could give us some sense as to what is driving those and what we should expect maybe in the next quarter or so.

And then separately if we were able to strip out, you know, what impacted the subprime margins, could you tell us where margins are today in terms of executions? And thirdly, if you could tell us or give us an update on your buyback plans.

ANGELO MOZILO: Let me just take the first part. On the prime, what is happening in the prime I think should be obvious to most observers, is that you have got -- you have had tremendous consolidation, a lot of people just going out of business who are just not participating any longer. You have acquisitions taking place of companies contributing to the rapid consolidation, more rapidly than I have ever seen and steeper than I have ever seen.

As a result, you have less competition and as Dave pointed out, rational competition. So when you have that, one is your margins are going to improve. There is no question that there are many players who have entered the business over the last five years that had to some degree or another irresponsible behavior, conducted themselves irresponsibly, and that impacted everybody, Gresham's Law.

But right now, you can see our pipeline increase dramatically, prime business. Margins increased and that appears at least to me at the moment to be a trend and one that we can see for the next several years. So that is our view of what is happening, and that continues, that trend, towards higher quality loans at better margins.

And as for the subprime, I will turn that over to David and let him walk you through that.

DAVID SAMBOL: Yes. Just to elaborate first on the prime side, Ken, the first quarter was characterized by very strong volumes and stable pricing margins. On the volume side, you know, we saw significant increase in refinance volume, more than offsetting the drop in purchase volumes stemming from slower housing activity. And if interest rates remain where they are today or drop, we expect this year to be characterized by strong refi volumes for the balance of the year.

And as it relates to top-line pricing margins, there was the absence of competitive worsening in pricing. So the outlook is very good for our prime business and prime margins. As it relates to subprimes, as I mentioned in my presentation, we are now pricing our rate sheets to provide for profitability in each of our channels, where I would tell you that in '06, for much of '06 and part of '05, competitive conditions were such that in certain of our segments, we were pricing to breakeven.

It was that tight, but with the exit from the market of so many players, we and the rest of the industry have materially increased rates. And starting as early as the first quarter, we expect to see each of our production divisions, our retail subprime operations, wholesale, and the little bit we still do on the correspondence side generating positive margins.

In terms of the levels, somewhere between net of expenses in terms of operating margins, somewhere in between 3/8 and 3/4 of a point is what we expect the pretax profit contribution to be on the volume, on the lesser volume that we will do.

KEN BRUCE: Great. And any comments or information you can provide on plans for share repurchases, please?

JOHN MCMURRAY: Ken, as you were asking about stock repurchase, as you know, we did $1.5 billion in November of '06. We are locked out for about another 45 days in connection with the accelerated share repurchase plan that we did. Management believes that we have significant excess capital. Our first priority would be to invest that business, that capital, in our existing businesses, but absent those opportunities we will aggressively manage capital and optimize it.

We are in the process of forging a consensus amongst the rating agencies right now, and we expect to have that resolved very, very soon. So that will be a developing story and we will probably have more for you at our next earnings teleconference call.

KEN BRUCE: Great. Thank you very much.

OPERATOR: Mike Vinciquerra, BMO Capital Markets.

MIKE VINCIQUERRA, ANALYST, BMO CAPITAL MARKETS: Good afternoon, gentlemen. Just a question

regarding the CLTVs that you guys report. Can you talk about how you determine your mark-to-mark CLTVs in your current portfolio? And then also discuss any changes in severity rates that you've seen over the last couple quarters when you actually do have to foreclose on a property.

DAVID SAMBOL: Okay. So first what we show, and I believe it is back on page 14, that is the current loan-to-value ratio, so it is not CLTV. So first, just to avoid any confusion, when we think of CLTV that is the combined loan-to-value ratio which would give effect to both the first and second.

What we showed for the HFI portfolio was the current LTV, so it would be just the first lien for those that were first liens, and then on the second it would obviously be combined. To update those to reflect current market conditions, we have several techniques.

The one that we used for this particular slide was applying an index that is done at a zip code level to each of the individual loans. So we looked at any amortization or balance increase in the case of option ARM and then took that, going back to the appraised value, updating it, using the indices and then recalculating the ratio for each loan and then aggregating that up into a weighted average. So that is the first technique.

The second is using an AVM, an automated valuation model, which Countrywide has their own proprietary model. That is also a loan by loan approach. Although it is not able to be used on every single property, which is why we will often use indices as well.

You asked about severities and the key thing that we are observing, the actual liquidation rates have been fairly stable. So by that I mean how many of the foreclosures roll through to REO. The timeframes though are starting to stretch out compared to what we have observed recently and so that is going to increase the carrying costs. But so far, not a drastic increase in severities yet.

MIKE VINCIQUERRA: All right. Thank you very much.

ANGELO MOZILO: You are very welcome. The answer to the question on 64 basis points, that is driven in the bank. The increase in spread is driven by the fact that the new assets that are being put on the balance sheet at a higher return than the old assets that were paid off. That is generally what has increased the spread, is the change in the quantitative aspect of the assets.

Let me just interrupt the question for a second. There was some discussion relative to, Ron, relative to spreads and what's happening in the market. You get a sense of what you see taking place. David alluded to spreads tightening in the BBB space. You've mentioned CDOs. Can you give us just a brief overview of what you see in the secondary market?

RON KRIPALANI, PRESIDENT, COUNTRYWIDE CAPITAL MARKETS, **COUNTRYWIDE FINANCIAL** CORPORATION: Absolutely. What we've observed in the last couple of weeks in particular and as a reflection

of the marketplace overall is that investors are looking at the following two things. One, an improvement in underwriting guidelines and tightening of underwriting guidelines and also a lesser supply. And as a result, in the last two weeks and in particular this week, we have seen investors come out of the woodwork and actually pay tighter spreads and start to see oversubscription on certain parts of deals at the bottom in terms of the credit stack. And so I think I expect that to continue.

We believe that, as we pointed out, if you have 25% to 50% lower volumes in subprime, therefore deals, and you have better quality vintage in 2007, I would expect us to have a stabilization if not tightening mode in the short term.

With respect to CDOs, as you might imagine in the first quarter, CDO machines came to a halting stop and the number of deals were put on hold or not done or warehouse lines were liquidated. That has shown some weakness and has continued to be weak, but I expect that as well to return to a healthier mode and perhaps a more consolidated mode and have fewer deals in the pipeline.

ANGELO MOZILO: Okay. Thanks, Ron. Next question.

OPERATOR: Seth Glickenhaus, Glickenhaus & Co.

SETH GLICKENHAUS, ANALYST, GLICKENHAUS & CO.: My questions have been answered, but I would just like to congratulate your team. I think you are doing a good job under the circumstances. Good luck to you.

ANGELO MOZILO: Thanks so much, Seth. I appreciate it very much.

OPERATOR: Paul Miller, FBR.

PAUL MILLER, ANALYST, FBR: Thank you very much. I wanted to talk a little bit about your servicing portfolio. The servicing value book again was up in the 170 level, but you did again -- I guess it looks like you are keeping back excess servicing, which you told us. But the multiple now is up to 4.4, which is the highest we have seen it in a very long time. Can you add some color on why you feel that the servicing -- that the new servicing valuations -- you believe in that 4.4 multiple?

DAVID SAMBOL: Okay, Paul. As you know, we have been retaining more excess servicing. There is a significant increase, almost 10 basis points from a year-ago level. In the fourth quarter, we retained 41.9 basis points. In the first quarter, we retained 40.5. I mentioned earlier in response to another question we have significant excess capital. We view that retention of the excess as an important way to put that capital to work.

We have observed spreads -- let's take WAC IO spreads from a tight of 500 let's say a year ago, over 1000 at this point in time. That is a level where we see ourselves as an investor. There is just not enough return to sell that into the market, so it conveniently works into our plans to put excess capital to work. There has been a slight

change in the mix more towards fixed rate product, which would also boost the multiple. In the aggregate, if you look at the multiple change from the fourth quarter to the first quarter, it's about 5% from 4.2 to 4.4, not a significant change.

PAUL MILLER: Will we see a better mix in the fixed -- as we see a better mix away I guess from subprime or more to fixed-rate loans, that supports a higher multiple basically?

DAVID SAMBOL: That's true. And keep in mind the aggregate portfolio multiple has been steady at 4.0 for the last three quarters.

PAUL MILLER: Yes, I know that, but I'm just -- but if the 4.4 does -- I just wanted to know where you come up with 4.4. I mean I understand completely that the fixed rate loans carry a higher multiple.

ANGELO MOZILO: Do you want to see the calculus of that?

DAVID SAMBOL: Well, no, Paul, this is Dave. It is not explained -- it is explained entirely by mix because the valuations were very similar in the fourth quarter versus the first quarter in terms of the yields at which we discounted future excess servicing cash flows. And so it is not explained for example by our tightening or becoming more aggressive in our OASs that we use to value the excess, which means that it is explained by mix.

PAUL MILLER: Okay. Thank you very much.

OPERATOR: Brad Ball, Citigroup.

BRAD BALL, ANALYST, CITIGROUP: Thanks. First, a question on the quarter and then a question on the guidance. John, could you give us a little more color on the policy behind the insurance reinsurance reserve release? Is that triggered by pre-payments or -- you said that it was driven by 2003 vintage release. Is that something that happens by the calendar and would we expect to get more of those releases going forward?

JOHN MCMURRAY: It is not by calendar. The key driver is the pool factor, so the percentage of loans that are still outstanding and so we have a specific threshold built into our policies that when the book year or the pool pays down to that threshold that we review it for a potential release.

And there will be -- there are going to be separate portfolios or reinsurance policies with each of the MIs and so they are not all going to hit that threshold at the same time. Some hit in the fourth quarter. Some hit this quarter. But that triggers our review and then what we will do to get further comfort is run stress scenarios to see how likely it would be for our entry point to be pierced and if that is at all likely, we would not release those reserves.

Also as I noted, we went and got an external insurance bid to reinsure the small exposure that we had just to see what an external bid would be for that remaining risk. So all of that combined together is what we used to make the decision to release those reserves.

BRAD BALL: So as we model out, should we expect you to go back to where you were last quarter or the year-ago quarter in terms of those kind of releases, the 5 million to 6 million range or can we sustain these high levels of releases going forward?

JOHN MCMURRAY: Well, if it were me, I wouldn't do that. I think the environment going forward is going to be more difficult than what we saw in the past. So remember when I covered that page, I said that the event space for a lot of these books, particularly 2002, 2003 were favorable, so that's prepayments, strong house price appreciation, a strong economy. For the newer books of business, it is unlikely that's going to have the same combination of favorable factors.

BRAD BALL: Fair enough. Real quickly on the guidance, so you know it appears that the lowering of the low end of your guidance is driven by the relatively lower production margins that you showed this quarter. You did bring the low end down to 10 basis points and you did 13 basis points this quarter. So is it reasonable to say that the 10 basis points, which would drive the low end of your guidance, is actually worse than conditions in the first quarter? And from some of the commentary you just gave, and I appreciate the comments Ron made, it sounds like things have actually stabilized and maybe there is prospects for improvement as the year progresses.

ANGELO MOZILO: Okay. As you know, Brad, our original guidance on production margins was 15 bps to 35 bps. Reacting to the 13 bps actual margin in the first quarter, we revised that down to the 10 bps to 25 bps that you referenced. That implies roughly 10 to 30 basis point margins the rest of the year, which is not all that dissimilar from the 15 bps to 35 bps that we started with with our guidance 90 days ago.

RON KRIPALANI: Having said that, I would agree with your characterization that there is reason to be optimistic based on data points that we look at today.

OPERATOR: Moshe Orenbuch, Credit Suisse.

MOSHE ORENBUCH, ANALYST, CREDIT SUISSE: Thanks. The subprime seconds that you retained, when were those originated. Were those relatively recent originations and could you talk maybe, Eric, a little bit about how you view that as a use of capital and whether it is something you are planning to do going forward.

ANGELO MOZILO: I'm going to bifurcate that question. Dave is going to take the first part of it.

DAVID SAMBOL: I could take both. They represent originations from 2006 that were unsold going into the first quarter and were particularly caught up in the liquidity and price deterioration that we saw in the first quarter and that is what motivated us to put them in HFI. It was simply a better investment where if we sold

them at current market prices, we would have been passing through yields that made much more sense to retain rather than to forgo.

As you might recall, I mentioned we are no longer doing subprime seconds in part because of the lesser investor demand for that product. Most of those seconds represented the 20% piece of 100% financing loans, the 80/20s that you might be familiar with that were very popular in the subprime market. Again, if you recall, we have materially curtailed our program such that we expect to do very few subprime 100% financing going forward.

So for all those reasons, I think what you saw with respect to the subprime seconds is somewhat anomalous and you shouldn't extrapolate that to future quarters.

As it relates to the capital allocation decision, unrelated to subprime seconds, we do, as Eric said, have significant capital excess we believe today. We are looking to invest that into our balance sheet and into our businesses first and foremost. The first place we look is in our HFI portfolio, residential mortgages.

As Carlos mentioned in response to another question, to the extent that we have not yet seen significant availability of residential loans in the market for sale that meet our return and credit risk criteria, we have elected to expand our security acquisition program. That is a place where we are allocating some capital along with excess servicing as Eric mentioned. Again, with respect to the securities purchases that the bank is doing, which is where we mostly focus on utilizing excess capital and deploying it, we are investing predominately in short duration, AAA quality mortgage-backed securities. Does that answer your question?

MOSHE ORENBUCH: Yes, thanks.

OPERATOR: Chris Brendler, Stifel Nicolaus.

CHRIS BRENDLER, ANALYST, STIFEL NICOLAUS: Hi, thanks. Good morning. Let's see, I want to ask a question on the residual valuation on page 12 of the slide deck. You actually show us the reserve. The estimate for losses going up sequentially from 23 -- 23 to 34 13. Just give us a sense of what drove the sharp increase in your loss estimates for your residual portfolio that has residual credit risk as you mentioned.

Was it delinquency trends within the quarter or is it more that in combination with some of the spread widening in the asset-backed market that impact your valuations at all and from a discount rate or any other impact?

Then probably the most important part of the question is what are you looking for and what is baked into your assumptions at this point for your residual portfolio and your entire credit risk exposure for housing prices? You've highlighted the fact that you've pulled back on first-time homebuyers that were a pretty big part of the subprime market. We already have I think a lot of supply out there. Foreclosures are going up. Underwritings being tightened across the board. What do you see for housing prices this year and the related impact on your credit exposure?

ANGELO MOZILO: (inaudible), what do you think about housing prices?

CHRIS BRENDLER: I think they are going to go down. I think it is a question of how fast -- how fast we can work through the supply, how willing sellers are to take lower prices. I think it will depend on just how this all plays out in the next couple of months.

JOHN MCMURRAY: Let me start with the last part of your question first. Like you, we expect house prices to be weak and in some markets down significantly. In fact, at some of the other presentations that we have done for you all, we have identified some of those markets for you where we expect to see not only significant weakness, but significant declines. So we expect weakness out for the next year or two, but then eventually house prices to start growing in line with income growth. Over the long term, housing prices tend to grow at a rate similar to what income growth -- so that is the answer to your last question.

With respect to the residual valuations, a couple key points. First off, these are held at fair value on the balance sheet. So in addition to the internal work we do to value these residuals, we also look to the market for indications of value and as Ron and other people have already -- Eric and Dave have pointed out during the first quarters, spreads widened significantly suggesting that investor yields were at and that by itself, absent even no other change, would result in a reduced valuation.

In addition to that, we took -- and I mentioned this on a couple of the slides -- we took our default expectation up. So for 2006, early 2007 and maybe even back into 2005, we expect those particular advantages to perform worse than what we originally expected. So we think there were additional fraud and other problems across the industry with those loans, so we took our default expectations up and that is largely what drove the difference between the $2.3 billion versus the $3.4 billion that you are referencing on page 12.

ANGELO MOZILO: I think bottom line is it's very difficult, as you I think alluded to, to determine where prices are going. We would certainly, based upon our view of where the world is today and based upon what you've said in increased foreclosures and that comes onto the market. We have to work through that during that period of time. In certain areas of the country, values will go down. There are certain unique areas of the country where they will stabilize and others, although a few, where values continue to climb, but not at the rate they did before. So it is sort of a mixed bag.

JOHN MCMURRAY: Let me also elaborate a little bit on the valuations. From my perspective, the future default rates embedded in our residual valuations are significantly greater than anything that we have observed empirically or historically, not only recently, but going back to the worst vintages that we're familiar with going back a decade. For example, the early 2000 vintage that was impacted by the recession at that time, saw defaults far lower than what we were projecting in the valuation of our current residuals.

The reason that our projections are where they are at and some might view to be conservative in fact, although only time will tell, relates in part to what we are observing with housing conditions the absence of home price appreciation as John mentioned and declines in some markets, but also based on the way the more recent vin-

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tages, '06 and late '05, have come out of the gate. So when we take a look at early delinquencies or what we call roll rates, loans transitioning from a current 30 day delinquent status or a 30 to a 60 status, initially in the early life of the '06 vintage, we observed that those roll rates were a fairly significant multiple to historical vintages. There was some degree of extrapolation of that multiple in our prospective valuation of default.

John mentioned in his presentation earlier the one data point that is important to point out and we think will increasingly be focused on by the market is that as we are seeing the '06 vintage season somewhat, now having almost a year, we are observing that relationship of delinquency roll rates or transitions converging with historical vintages, which suggests that there is a possibility that extrapolating this very early experience in a way that the market has and the way to some extent we have in our valuation hopefully might prove to be conservative.

I think John characterized it as rather than experiencing significantly higher cum losses in the aggregate, that what we may be experiencing is a front-loading of the losses where the worst loans originated are identifying themselves, going bad and then what remains now that hasn't gone bad after a year of seasoning will perform more closely to prior vintages. So those are some data points in fact if you are trying to size up the risk in our residuals that are relevant to reflect on.

CHRIS BRENDLER: I appreciate that. That's good color. Just one quick follow-up, if I could. Do you have any assumptions or any color you can add related to credit on the reset issue? There has obviously been a lot of focus on this for the last couple of years. Now it is sort of coming to a head and there has been a lot of discussion about loss mitigation, forbearance programs. I think, Angelo, you mentioned about helping the borrowers and I totally agree, but what are you expecting for that this year and how does it factor into your residual and other credit exposures?

ANGELO MOZILO: We have done -- you know with that backdrop, we are going to do everything we can to keep these people in the homes. That is our obligation, including we are trying to move mountains in terms of getting the GSEs and others to assist to carve out programs, pre-existing programs that have now been taken away, to reinstate those programs to create a bridge for these people to get to the other side of this raging river. Not in terms necessarily of new purchases, but at least in refinances.

These people bought these homes under certain rules, now the rules are being changed in the middle of the game on them. So we are working from a policy viewpoint, from a -- well, not from a legislative viewpoint, from a policy viewpoint, from a regulatory viewpoint, working with the GSEs and with others to see if we can assist these people through a refinance to keep them in the home.

In terms of the whole reset issue, David has done an extensive study of that in terms of the timing and depth of that issue at least as it relates to Countrywide and I would like for Dave to comment on that.

DAVID SAMBOL: Yes, I think it is a couple of things that are relevant to point out. First of all, it might be interesting for you to know that of the foreclosures that we have seen to date, we, in the last year if you will, we go through a good deal of analysis to try to understand the driving cause for the foreclosure for somebody losing

their home and I can tell you that the percent of foreclosures attributable to payment increases associated with ARM resets is extremely nominal, excuse me, immaterial. The vast majority of the foreclosures relate to a change in the person's income rather than the payment going up as a result of loss of employment or divorce or death. While we are concerned about the impact on future defaults associated with ARM resets, it has not explained to any extent historical defaults.

In terms of the impact on our residual valuations and losses, it is our belief -- Angelo mentioned we do a lot relative to our workout programs to ensure that if a borrower, if a family has a desire to stay in the home and if they have income such that they were able to afford the payment and were making the payment before the ARM reset, we believe that our workout programs are such that, for the most part, we will be successful in keeping them in the home, avoiding a foreclosure and avoiding the loss. So with respect to our own loss exposure applicable to reset -- solely to reset that factor, we don't ascribe a significant materiality to that.

CHRIS BRENDLER: Okay. I would agree. Thanks for your time.

OPERATOR: James Fotheringham, Goldman Sachs.

JAMES FOTHERINGHAM, ANALYST, GOLDMAN SACHS: Thank you. Angelo, just further to your comment at the beginning of this call that a legislative solution for the mortgage predicament is neither necessary or appropriate. I understand and respect that this is your view of what ought to happen, but I am just as curious to hear what you believe practically will unfold. What do you believe is the most likely legislative solution here and what is the most likely timeframe for enactment? Thanks.

ANGELO MOZILO: Well, I don't and I don't know how much of this is really coming from a base of knowledge or a base of hope, but I don't, as I noted in my comments, I don't believe legislative solution is appropriate from a couple of perspectives. I have been on this earth a long time and every time there has been a serious issue in this country, whatever it might have been and legislation passed during the heat of those issues, is always bad legislation, always bad legislation. No different than a business decision being made in panic and that is number one.

Two is I think from every angle I have gone at this issue and this really touches the heart of the mission of Countrywide and why Dave and I started this Company is I think -- I am absolutely convinced that any attempt to do anything legislatively is going to exacerbate the problem and foreclose people who should own homes from owning homes and secondly, accelerating the foreclosure issue. I have studied every proposal made. I've had our people intimately involved with Senator Dodd and his committees.

As I said, I am very grateful that he is brought people together and I think at the end of day, at least what I have read and what we have heard from Senator Dodd is that he doesn't believe that a legislative solution is the ultimate resolution here.

And it is the issue, if I can just impute this into my comments, it is an issue of responsibility. Lenders have a re-

sponsibility to make sure that they are disclosing all risks to the borrower. On the other hand, the borrower has a responsibility to make sure that they are making the right decision for them and their family and all of this has to be taken into consideration as we go through this process.

I think that if you have, as Dave pointed out, borrowers who want and desire to stay in that home, who have some ability to make reasonable payments, that the industry can work this through with them and that the country and the homeowners and the people most impacted, lenders and borrowers, will be better served if we can work out this together without legislative interference.

Now I do -- I have said that I believe that regulatory relief on some of the programs that have either been absolutely destroyed and in ones that have been tempted to change dramatically such as hybrids coming under regulatory guidance proposals that I think are unreasonable should be addressed so that we create liquidity in the times that liquidity is most needed and not to extract liquidity from these homebuyers when they need it the most.

So I would rather see that type of solution rather than a legislative solution. I am comfortable, at least at this moment, that everybody has gotten the word. There are people who want to -- you know I have seen certain proposals by other senators to put in -- put through some legislation. I don't think based upon Senator Dodd's current comments that legislation is going to pass nor should it pass and I think we can work through this without it a hell of a lot better than if they did something.

JAMES FOTHERINGHAM: Thank you very much.

OPERATOR: James Shanahan, Wachovia.

JAMES SHANAHAN, ANALYST, WACHOVIA: Hello, everyone. Thanks for taking my call. On page 7 of the presentation, there is a disclosure about the ABX hedge gain, $149 million. This is verse the revenue impact of $400 million reported for subprime. I am curious if that hedge gain is based upon -- is a realized gain based on closing out the positions or if it is a -- if it is a mark-to-market gain.

KEVIN BARTLETT, CIO, **COUNTRYWIDE FINANCIAL** CORPORATION: This is Kevin Bartlett. A portion of it is closed out and a portion is not. We do have a remaining position in the ABX index, but a good portion of that gain is closed out.

JAMES SHANAHAN: So given the sort of recovery in the ABX index, I suspect that quarter to date, there would be a loss on that hedge position?

KEVIN BARTLETT: Not really much. At the current time, I think the ABX is -- contrary to what you said, the one we focus on the most is the [071B-, BBB-]. It is only about five points up off the lows of that index. It is actually down for this month today.

UNIDENTIFIED COMPANY REPRESENTATIVE: The only loss would be (inaudible) wouldn't it?

ANGELO MOZILO: That has nothing to do with this.

KEVIN BARTLETT: So anyway, most of the ABX gain or a good piece of it is closed out, but there is an open position.

JAMES SHANAHAN: And an easy follow-up, are all of the HFI loans classified as available for sale or are any of those classes held to maturity?

JOHN MCMURRAY: Remember -- so on loans, it is HFI or HFS. Those are the only two classifications available for whole loans. It's securities that are trading available for sale and held to maturity.

KEVIN BARTLETT: HFI is synonymous with held to maturity.

JAMES SHANAHAN: Got it. So would the HFI loans then be -- would be held at market value in every case?

JOHN MCMURRAY: They are held at amortized costs.

JAMES SHANAHAN: So if you transfer a loan from HFS to HFI and there is -- it sounds like you took a part of that impairment and value this quarter, but would we see -- what would it take to put all those loans back at market value sort of today?

UNIDENTIFIED COMPANY REPRESENTATIVE: The accounting is is that if you are originating a loan with the intent of holding it for investment to maturity, it is held at cost to the typical bank balance sheet. If you are moving loans from an HFS to an HFI category as we did with the seconds we discussed, the accounting there is they are moved in at market. So you have to take an impairment first to market and then you move them into HFI and then thereafter they are accounted for just as HFI loans would that were originated with the intent of being put into HFI initially.

JOHN MCMURRAY: That is the basis adjustments that we talked about during my presentation that we will take when we are moving repurchases or loans from inventory over into the portfolio.

JAMES SHANAHAN: Thank you. And so the HFI value after you have transferred them represents sort of an updated cost basis. They will be held --.

JOHN MCMURRAY: Yes and market.

UNIDENTIFIED COMPANY REPRESENTATIVE: It is a lower cost to market is what it represents.

JAMES SHANAHAN: Okay. Thank you.

OPERATOR: Ron Mandle, GIC.

RON MANDLE, ANALYST, GIC: Thanks very much. I had a question about the earnings guidance for earnings per share and that was if I take the first quarter, the $0.72 and then you identified $0.56 of special factors and mainly write-downs, but also the reserve release in insurance and if I added that back and said, well, that is my run rate going forward and use that for the remaining three quarters, I would get something above the high end of your earnings -- EPS earnings guidance for the year. So I am wondering what the other factors are you may be thinking of that are leading you to the lower level.

ANGELO MOZILO: Well if it was that easy, we wouldn't need these earnings calls.

RON MANDLE: That's right and we should all be so lucky.

ANGELO MOZILO: So I think -- why don't you go through some of the factors in terms of what is going to impact future earnings.

DAVID SAMBOL: Well, it's true that certain of the losses that were the subject of our discussion here on this call and in the press release, we are hopeful are not recurring losses, that the subprime is behind us and some of the credit loss provision increases, as Carlos suggested, might not recur if things don't get worse. But there are other things applicable to the quarter such as we had a very, very strong performance in the servicing segment in the MSR portfolio as you might have noted from the press release. We can't necessarily -- there is uncertainty as to how the MSR asset will perform and of course, there is a lot of environmental uncertainty and we reflect on the range of possible performance resulted in our arriving at the range that we did.

RON MANDLE: So basically you are concerned that some of the other factors might get worse even as some of the credit factors hopefully won't be so negative in coming quarters?

ANGELO MOZILO: Or get better. You know your margins can improve, volumes can improve. A lot of factors can go either way and that's why we're here trying to manage this every hour of every day to make sure that we get the best results out of the events that are taking place. So there are events balancing both sides. I would say that as I view it, there are many factors on the plus side of the equation today as there are on the negative side of the equation.

UNIDENTIFIED COMPANY REPRESENTATIVE: And I wouldn't characterize it as a concern. In fact, we are cautiously optimistic, but there is a lot of moving pieces as I'm sure you know environmentally that could impact us.

RON MANDLE: Right. I was just trying to see if there was anything that I had overlooked in that regard and I appreciate your comments. Thanks very much.

OPERATOR: [Rajiv Patel], [Sonova Capital].

MICHAEL COHEN, ANALYST, [SONOVA CAPITAL]: It's actually [Michael Cohen]. Rajiv had to hop off. I was just wondering -- I had a question and I know you preliminarily addressed this with Chris Brendler's question, but of the $363 million of provision related to the residual, how much or in dollar terms was related to spread widening and how much was related to credit provision, changes in credit assumptions?

DAVID SAMBOL: I don't think we are in a position to break that out here and give you that level of granularity, but I would emphasize as well -- I mean you see what we are providing for in cumulative losses. And as John mentioned on the '06 vintage for example, it exceeds 7% remaining losses, which if you divide that by a severity assumption, you would see that the default rates implicit in that are very -- I don't want to say very conservative, but higher than anything we have seen.

At the same time, we did provide for -- in the valuation for spread widening such that the ROEs that we expect, assuming the cash flows are no worse than what we have provided, should equal or exceed 15% ROE on that investment for us, making it arguably a more attractive investment prospectively than it has ever been. Wider yields and more conservative cash flow projections.

MICHAEL COHEN: Okay, thank you. I guess you guys also talk about your sort of excess capital position and how you -- how do you sort of arrive at that? I mean for lack of a better way of saying it. I mean is there a way that you guys can provide a framework for investors to sort of evaluate your capital position so that we can kind of calculate to it and project it out on a go-forward basis?

ANGELO MOZILO: Okay. In response to that question, let me point out that we have been putting a significant effort into developing economic capital protocol and we started to roll out some disclosures in our 10-K this year about that. That process continues under the leadership of Kevin Bartlett and we will have further rollouts during the year to give you some view of what management believes the capital required to manage our business is.

At this point in time, we are significant users of unsecured commercial paper and medium-term notes and that brings the rating agencies into play and we are working with them to forge a consensus amongst the way they view the capital required to run our businesses. So in essence, you can look to them today to be the operative constraint in terms of the capital that we need to run our business.

Our economic capital would be less than what they see as necessary to be the capital required, but from time to time at investor forums and things like that, we actually go through very detailed calculations and show you where we see these capital cushions. So I would urge you to refer back to those and stay tuned for future investor forums and like presentations where we will give you more insight into where we see our excess capital.

We are at a pivotal point right now in terms of bringing all three credit rating agencies into focus and we should have something for you relatively shortly on that.

MICHAEL COHEN: Okay. So essentially is your projection then that -- I mean because if you say sort of the economic capital versus the rating agency capital, that is sort of your view of risk, but if their view of risk is different then their view -- then your view of risk and theirs is the binding constraint, then i.e. economic capital is actually higher than you think it is until you can convince them otherwise. Is what you're saying that you are in the process of having convinced them otherwise?

DAVID SAMBOL: Well, this is Dave. It is the case that we calculate our capital needs based on economic capital framework and under that framework, we have a far more significant amount of excess capital than what the rating agency models would suggest or even what regulatory capital requirements are and as Eric said, the operative constraint is the rating agency. Each of them has a model themselves, which you know we either have or we have data that allows us to emulate how they look at us and we take the most conservative results of those three models and that becomes our operative constraint.

To the extent that there is an outlier or one of the rating agencies has a more conservative view of capital than the others, we are always working to bring them in line with each other and then collectively to bring them in line with our view as to the true economic capital needs of the Company and we are making progress and have made progress.

It's a result of in part that progress that we have communicated, that we have -- our view operatively is that we have excess capital on top of the fact that the balance sheet has not been growing at the pace that it has in the past. So that is kind of a summary as to the topic of excess capital.

UNIDENTIFIED COMPANY REPRESENTATIVE: Furthermore, Michael, you, David and I have all referred to the rating agencies as the operative constraint, but we have already disclosed that we are working on integrating our mortgage company in our bank and our reliance on that unsecured commercial paper and medium-term notes will decline over time thereby reducing the importance of that operative constraint today at the rating agency.

ANGELO MOZILO: I would just suggest based upon your question and the direction of your question that I think it is best that we will have a clearer picture two or three or four months from now than we have today, particularly as it relates to the rating agencies and I think at that point of time, we will be able to answer your question with much more clarity than today.

MICHAEL COHEN: Great. Thanks, Angelo.

ANGELO MOZILO: Thank you.

OPERATOR: Greg Lapin, Tribeca.

GREG LAPIN, ANALYST, TRIBECA: The only question I would ask is on the servicing operation. What caused the lower earnings on escrow balances this quarter versus the run rate that you had for the last few quarters in light of the short-term interest rates not moving much?

ANGELO MOZILO: Our balances were down and there were fewer days in the quarter to earn interest.

GREG LAPIN: Okay. So you think they'll --.

UNIDENTIFIED COMPANY REPRESENTATIVE: The balance is down because of tax payments.

GREG LAPIN: Is that a magnitude -- do you think it will recover to the level --?

UNIDENTIFIED COMPANY REPRESENTATIVE: It's probably driven -- you will have dips in that escrow balance at least twice a year depending upon what states we're operating in, what counties, but as primarily tax payments drive it down rather dramatically at periods of time and then they will ramp their way back up again. So I think you've got to look at it over -- I think just look at the quarter -- could distort your conclusions. I would just watch it over 2000 -- over the balance of this year, assuming that the rate -- the rates stay stable, you should see increased earnings in the -- out of the escrows because they will grow as the portfolio grows.

GREG LAPIN: Okay. So it moves it back up. Thanks. You know, just one more. You touched on it a couple of times, the theory about the front-ending of credit emergence equating to probably potentially a similar cum loss rate and then the second time you talked about it, you went a little bit further. Can you go a little bit more? You said that the -- just to support that --.

ANGELO MOZILO: You remind me of my mother. It's never enough.

GREG LAPIN: So the roll rates converging, I think you got to and in my head, I just think about -- there is credit extension of borrowers that shouldn't have qualified, so maybe they might not be the same borrowers that let's say on month 25 start to default and so then with all the frequency, you end up with more in total. I wanted to hear that and maybe how long -- how many more months or periods should you wait to be more conclusive on whether this is evidenced or not?

UNIDENTIFIED COMPANY REPRESENTATIVE: You know absent a crystal ball, you know we don't know what is going to happen, so it is all speculation. We can only comment on empirical observation data points. This is what we -- you know what we covered in our earlier responses, but every quarter and every month, you know we have another quarter of empirical data, which we consider in our updated valuations for that quarter.

We are hopeful that when future data points come in, it would suggest that the outlook is less bearing than what we have provided for in our current valuations, but the possibility exists that things could look worse too. But we really do study empirical data and performance to a great extent and arriving at the valuations that we think based on all the data available to us is appropriate.

OPERATOR: Mr. Lapin, your line is open.

GREG LAPIN: Can you share that with the -- do the rating agencies come up with something similar? Is this more of an internal analysis, more on the front-ending?

JOHN MCMURRAY: This is John. We do share some of our internal analyses with the rating agencies, particularly where our view diverges from theirs. So if we think there are certain attributes or other factors that they are looking at too favorably, we would like them to know that. I think that is the best thing for the overall market.

UNIDENTIFIED COMPANY REPRESENTATIVE: Let me point out that we try as well to take a look at what other people have and other people's models, other people's valuation and cum loss projections and from data publicly available to us, it appears to us, and I am sure you have this information as well, that the cum losses that we provided for probably on the high end of what we have seen disclosed others provide for.

But remember at the end of the day with respect to this particular asset, our subprime residuals, which is up to 300 some odd million assets on our balance sheet, all the analysis then has to be adjusted based on what we view market is and that is in control. So mark-to-market assets.

GREG LAPIN: Great. Thanks for rounding that out and for letting the call go on so long.

OPERATOR: [Nick Elsner], Wellington Management.

NICK ELSNER, ANALYST, WELLINGTON MANAGEMENT: Thanks very much. If we could just briefly go back to the capital question. I just -- I thought I heard you mention there may be less reliance on MTNs and unsecured funding, that that will decline over time. I guess I just wondered your overall use of secured funding versus unsecured. Should we expect that to change at all going forward? If you could you put some numbers to that, that would be help.

UNIDENTIFIED COMPANY REPRESENTATIVE: We don't have numbers to share with you here, but you should know that one of the aspects of our strategic plan is to migrate increasingly some of our mortgage operations in CHL into the bank, into the legal entity, which is the bank and as we increasingly do that, we intend to begin retaining residual investments from our mortgage banking activities, notably MSRs and residual securities on the balance sheet of the bank and then to fund that balance sheet with deposits and home loan bank advances and traditional bank funding strategies.

That, we began -- we believe and intend will begin occurring in 2008 and as that happens, our balance sheet of less liquid assets such as MSRs and residuals, which are funded with unsecured or capital market debt, will lessen and ultimately, we are hoping the remaining reliance on capital market debt will be negligible at least as it relates to the funding of mortgage-related assets. But specific numbers, you know we do not have to share with you at this point.

NICK ELSNER: Thank you. I guess one more -- one more thing. I notice in your 10-K, you disclosed that you have applied to change the bank charter to a thrift charter. Just kind of wondering if the thought process behind that in terms of the OTS having somewhat less stringent capital requirements and so forth, could you just sort of provide a little color on that?

ANGELO MOZILO: It had nothing to do with that. We have excess capital. That decision was made because of I think two primary reasons. One is that the OTS has an historical housing mission and that matched up with our mission much better than the OCC and the Fed. We had no particular complaints about the Fed at all nor the OCC. We believe we enjoyed a solid relationship with them, but the practical matter was that when we began to examine where this Company was going over the next decade and beyond, we did not see ourselves in any business that would require an OCC charter and Fed supervision. We know we're not going to be a lender in commercial loans in Japan or any of those kinds of things. So the businesses that we plan to be in matched up perfectly with the authorities at the OTS.

The second reason, which is tied to that, is that it is much more difficult, at least for us, to manage and deal with two regulatory bodies that from time to time went in two different directions than it was to deal with a single regulator that examined the bank and supervised the parent.

And so for you know for operational reasons and for cost factors to our shareholders, we felt it was in the best interest of the Company to transition, and only for those reasons, transition from OCC Fed to the OTS, which has been completed. Now that we've planned to do it, we have done it.

NICK ELSNER: Thanks very much.

OPERATOR: Ladies and gentlemen, thank you very much for your robust questions and interest in the call today. However, Mr. Mozilo, with a quick look at the clock, I believe we are out of time for today. I will turn it back to you for any closing remarks.

ANGELO MOZILO: Thank you very much, Brent, and thank you for your participation and we look forward to speaking to each of you in our next quarterly call. Thank you very much.

OPERATOR: Ladies and gentlemen, Mr. Mozilo is making today's discussion available for replay through 11:59 p.m. Pacific Time on May 10, 2007. The replay dial-in number and access code are 800-475-6701, 868872 and internationally 320-365-3844 again with the conference ID of 868872. And that does conclude our earnings call for this first quarter. Thank you very much for your participation, as well as for using AT&T's executive tele-

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